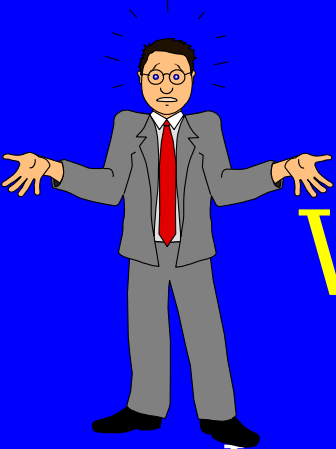


# SUBCONTRACT PRICING AND NEGOTIATIONS

By  
DON WHITING  
SFA Pricing  
Dec 30 1999



# What good does it do?

- I can't fight "privity of contract", can I?
- Reveals level of subcontract risk
- Provides input to award fee determinations
- Provides input to PCO readiness reviews
- Lessens EVMS surveillance of subcontracts
- Assists prime and subcontractors in disciplining their internal operations
- Contributes to prime contract negotiations

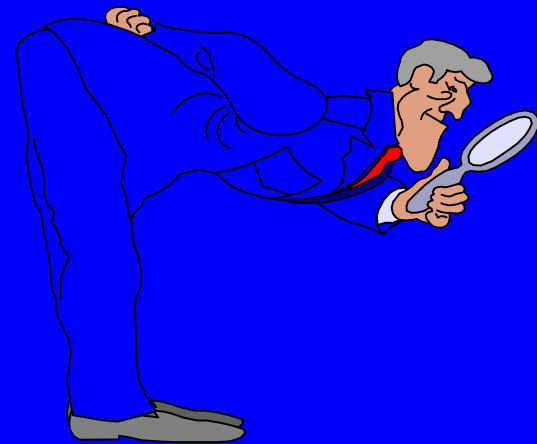
# Subcontract Pricing:

## Agenda

- When does DCMA review subK pricing?
- Cooperation (Teaming)
- Prime Contracts vs Subcontracts
- Truth in Negotiations (TINA)
- Cost Accounting Standards
- Subcontract Competition
- Price Analysis
- Cost Analysis
- Subcontract Negotiations

# When Does DCMA Review Subcontract Pricing?

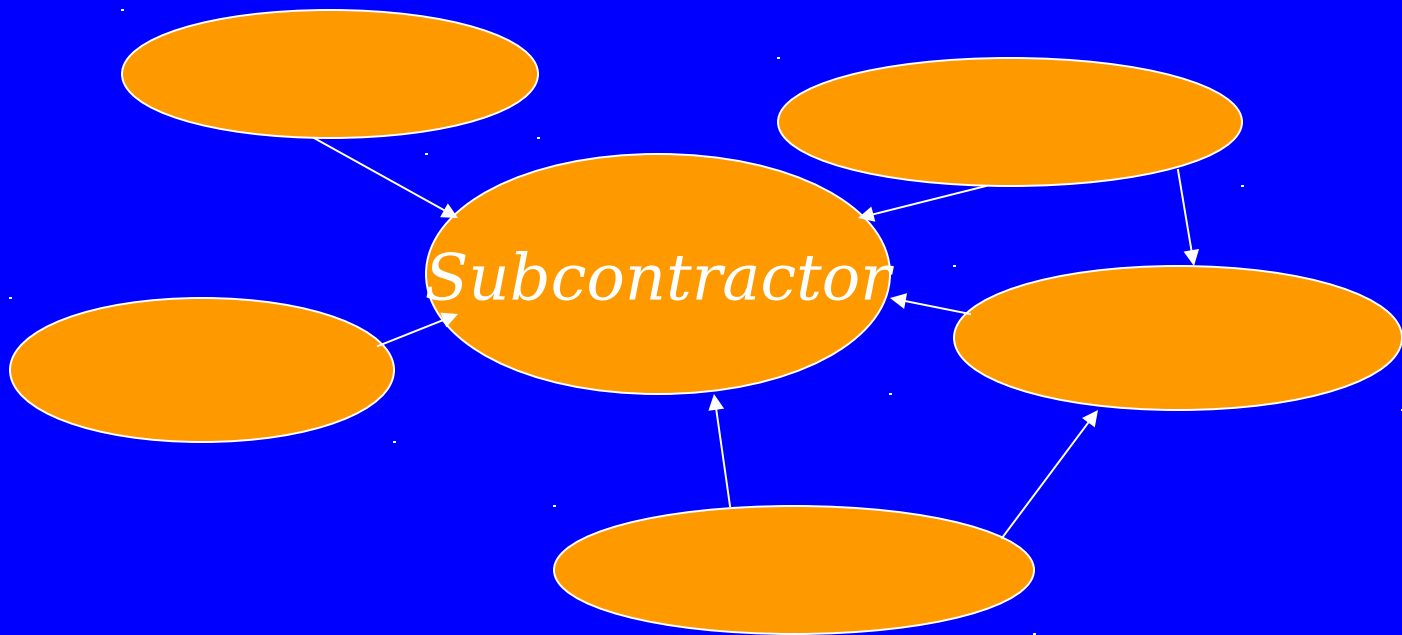
- PCO delegation
- Delegation to subcontractor CMO
- Advance notification of subcontract award
- Consent to subcontract award
- Contractor Purchasing System Reviews
- Self governance validation
- DCAA operations audits
- Congressional inquiries



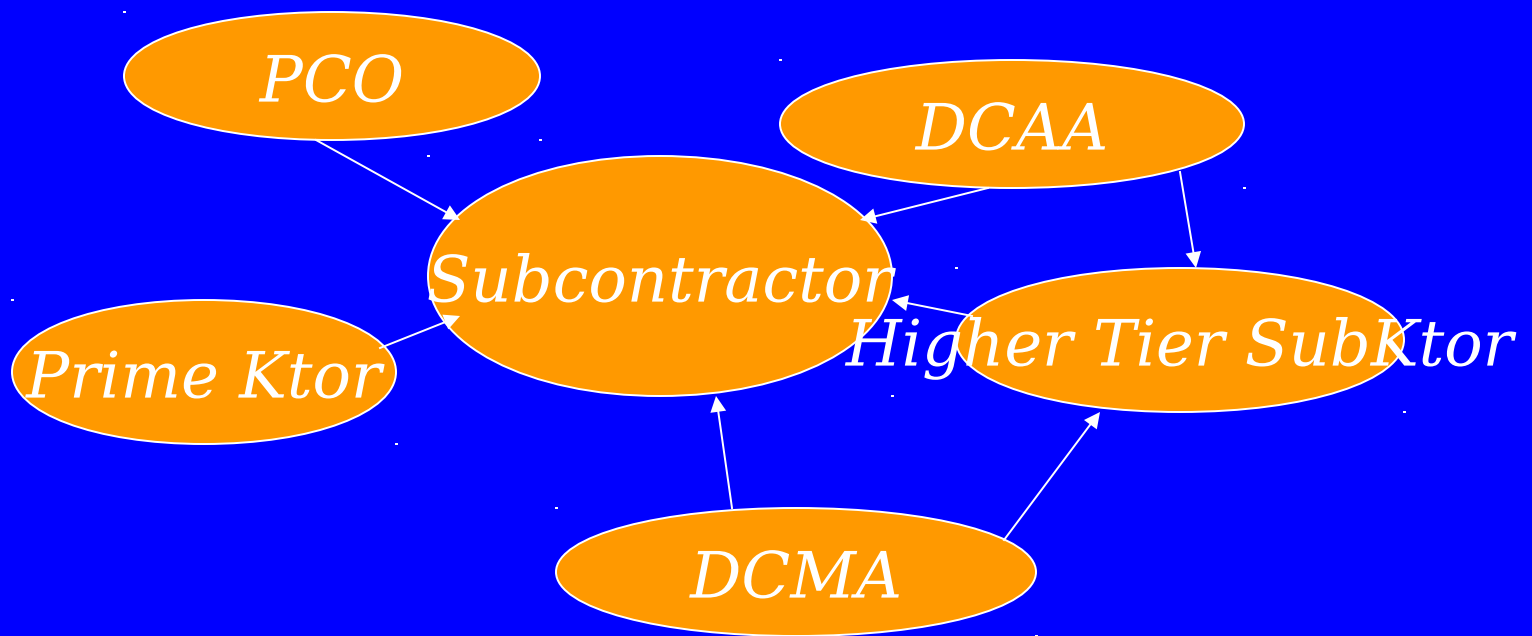
# When Does DCMA Review Subcontract Pricing (continued)

- EVMS submissions
- Award fee determinations
- Customer requests
- Defective pricing and fraud cases
- Terminations for default and convenience
- Prime contractor requests for subcontract TINA waivers

# Cooperation (Teaming)



# Cooperation (Teaming)



# Prime Contracts vs Subcontracts

- Prime contracting principles apply to subcontracting
- Additional principles apply, too
  - Uniform Commercial Code (UCC)
  - State Law, etc.
- Prime contractor enforces Gov't policy on subcontractors and ~~sub~~ subcontractors





# Truth in Negotiations (TINA)

- Waiver of prime contractor cost data waives all subcontractor cost data? NO WAY!
- Only the HCA can waive TINA for subcontracts



# Truth in Negotiations (TINA)

- Subcontractor Cost Data Requested When?
  - Submitted to PCO if >\$10 million
  - Submitted to ACO with advance notification & consent
  - Retained for Government audit if >\$500,000

# Truth in Negotiations (TINA)

- TINA not applicable to
  - Capital equipment and indirect items (except at GOCO operations)
  - Commercial items
  - Some MMAS (ERP) systems requisitions
  - “Risk” purchases (in advance of prime contract award)

# Truth in Negotiations (TINA)

- Who obtains it?
  - Purchasing departments
  - Major subcontracts departments
  - Contracts (marketing) departments

# Truth in Negotiations (TINA)

- Other considerations
  - Certificates of Current Cost or Pricing Data
    - Not usable if submitted in advance of negotiations
    - To be resubmitted at conclusion of negotiations
  - MMAS peculiarities
    - Related line items
    - Split awards
- Dept. of Energy Prime Contractors

# Cost Accounting Standards (CAS)

- Applicability to subcontracts
  - Almost the same as TINA
  - Small businesses exempt

# Cost Accounting Standards (CAS)

- Other considerations
  - CAS disclosure statements
  - CAS certificates apply to instant subcontract
  - The “disputes” paragraph of the CAS clause
  - “Negotiated subcontracts”
  - MMAS systems
  - Notification to subcontractors’ ACOs
  - ACOs include subcontracts in impact eval.

# Subcontract Competition

- FAR 52.244-5 requires competition to the maximum practicable extent
  - May conflict with “Best Value Subcontracting”
  - Dual or multiple source funding
  - “Recommended” vs directed sources
  - “Make” items (affiliates & subsidiaries vs outside suppliers)



# Private Company Pricing Techniques

- Comparison of competitive quotations
  - Ensure that terms and conditions are the same
    - Sales orders = counter offers
    - Refer counter-offers to Legal Counsel
  - Account for differences in delivery schedules
  - Consider effect of discounts and delivery mode

# Private Company Pricing Techniques

- Peculiar industry pricing practices
  - “Pittsburgh Plus” pricing for steel products
  - Non-deliverable buyer owned property
  - Letter subcontracts
  - Traveling requisitions
  - Plus or minus quantities

# Private Company Pricing Techniques

- More peculiar industry pricing practices
  - Purchasing pre-owned/used products
  - Most favored customer clauses
  - Forging services
  - Make-or-buy

# Private Company Pricing Techniques

- More peculiar industry pricing practices
  - Transportation costs
  - Delinquency recovery
  - Qualifying competitive sources

# Private Company Pricing Techniques

- Price history analysis
  - Ensure previous prices were reasonable
    - Verify quantity comparability
    - Similarity of manufacturing processes
    - Warranties
    - Non-recurring vs recurring costs
  - Request in-house evaluation of effects of above
  - Account for inflation
    - Producer Price Index (Consider index lag time)
    - DRI rates

# Private Company Pricing Techniques

- Learning curves
  - Continuous vs broken production
  - Commercial item vs built to print
  - Select appropriate slope
    - Price improvement curve tables by commodity
- Teaming Agreements

# Private Company Pricing Techniques

- Independent in-house estimates
  - Industry rates (not buyer's rates)
  - Identify differences to be negotiated
- Parametric analysis
  - Material and labor estimates done separately
  - Determine measurable characteristics
- Corporate/Group purchase agreements

# Private Company Pricing Techniques

- Commercial catalog item prices
  - Substantiate commerciality with 3 recent sales
  - Research similar items from other producers
  - Determine quantity price breaks
  - Request supplier to justify difference in price from those of similar items, or
  - Request in-house estimate of differences in price



# Common Price Analysis Problems

- Technical personnel
- Circular analysis
- Consultant agreements may not be subKs
  - Direct charge?
  - Definitive scope of work?
  - Enforceable termination for default clause?

# Common Price Analysis Problems

- Prompt payment discounts
- Late CFM
- Non-economic ordering quantities
- Stores replenishment intervals
- Incorrect subcontract terms and conditions
- Overage subcontract UCAs

# Common Price Analysis Problems

- Prime contractor small purchase dollar limitations:
  - Simplified acquisition threshold? No!
    - Risk Analysis
    - Varying documentation requirements
- Control of petty cash funds

# Common Price Analysis Problems

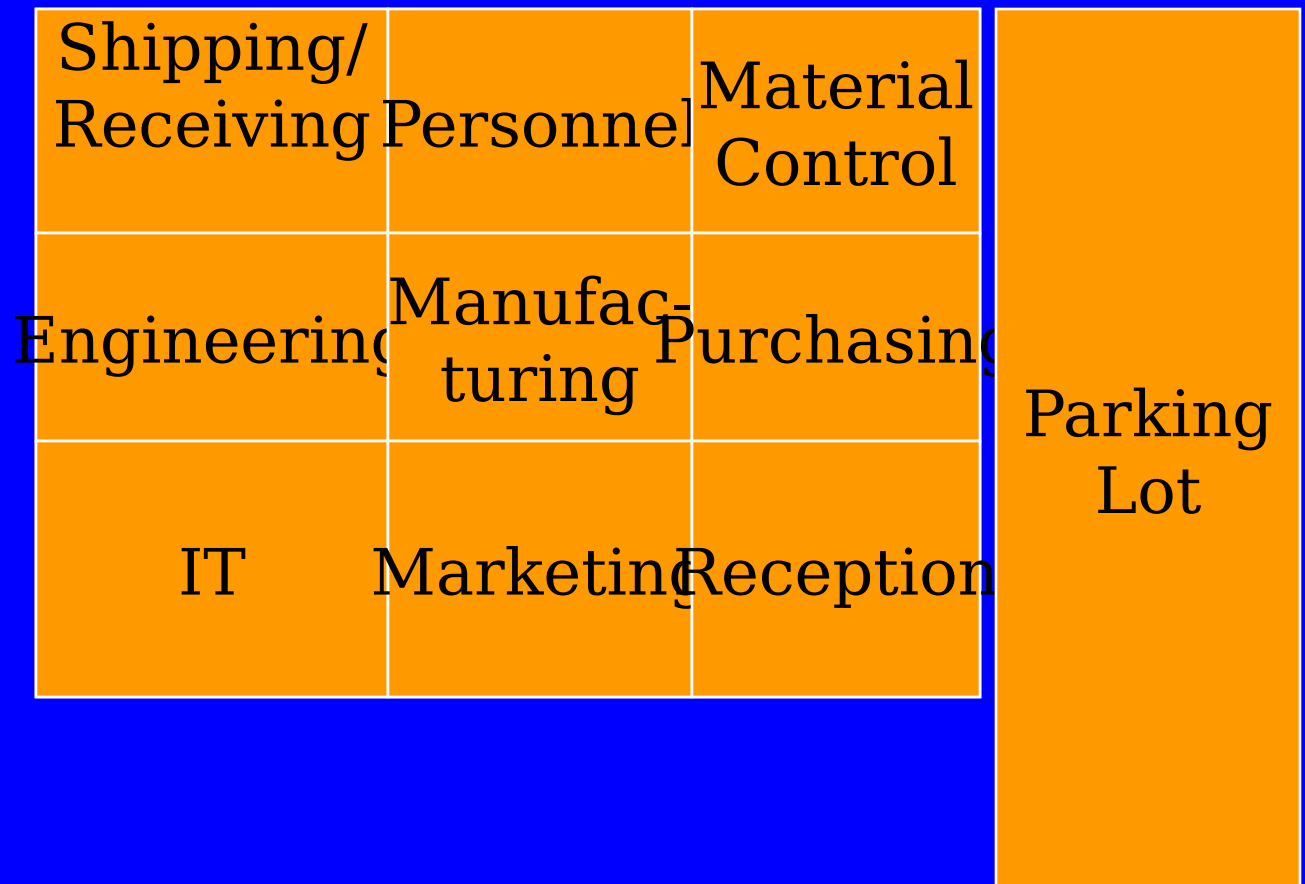
- Change orders
- Precious metals retention

# Common Price Analysis Problems

- Types of commercial pricing vehicles
  - Federal Integrator Agreements (FIAs)
  - Government Development Product Agreements (GDPAs)
  - Volume End User Agreements
  - Corporate Pricing Agreements
  - Original Equipment Manufacturer Agreements (OEMs)

# Common Price Analysis Problems

- Fraud? (Subcontractor Kickbacks)



# Common Price Analysis Problems

- Less well-known fraud Indicators:
  - Manipulated commodity assignments
  - Overuse of dealers vs manufacturers
  - High numbers of low dollar value part numbers
  - MMAS system allowing only one part number
  - No long term supplier agreements
  - Buyer initiated single source purchases
  - High volume of subcontract change orders
  - Buyers turn down promotions

# Common Cost Analysis Problems

- Subcontractors refuse prime contractor access to cost records
- Disuse of subcontractor EVMS reports
- DCAA assist audits



# Subcontract Negotiations

- Negotiate with low bidders vs award without negotiations
- “Trade discounts” vs “prompt payment discounts”
- Weighted guidelines not required

